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IN THE

Supreme Court of the United States

OCTOBER TERM 1957.

No. 389

JOSEPH N. ROMM AND HELEN K. ROMM, HIS WIFE,
Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH JUDICIAL CIRCUIT

WARREN W. GRIMES,
Shoreham Building,
Washington 5, D. C.,
Counsel for Petitioners.

Of Counsel:
HORACE J. DONNELLY, JR.,
Shoreham Building,
Washington 5, D. C.

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COMMISSIONER OF INTERNAL REVENUE, *Respondent*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH JUDICIAL CIRCUIT

To The Honorable, The Chief Justice and the Associate Justices of The Supreme Court of the United States:

1. Joseph N. Romm and Helen K. Romm, his wife, respectfully petition for a writ of certiorari to the United States Court of Appeals for the Fourth Judicial Circuit, which affirmed in part and modified in part a decision of The Tax Court of the United States involving income tax deficiencies and civil fraud.

I. OPINIONS BELOW

2. The opinion of said Court of Appeals appears in the advance sheets for 244 F. 2, No. —. The Tax Court's memorandum opinion is in 15 TCM at 526. Both are reproduced and are appended hereto.

II. JURISDICTIONAL STATEMENT

3. Jurisdiction here is invoked under 28 USC sec. 1254 (1); Act of June 5, 1948, c. 646, 62 Stat. 928. The judgment of said Court of Appeals sought to be reviewed was entered May 27, 1957. Record p. 65.

III. QUESTIONS PRESENTED

4. (a) Did the Tax Court lack jurisdiction where the Commissioner of Internal Revenue conceded error in issuing the statutory deficiency notice against husband and wife as jointly and severally liable for income tax deficiencies and penalties?

(b) Did the Court of Appeals have power on mandate to order the Tax Court to correct its "undoubted" error and to reissue its decision against only one of the parties to the action?

(c) If (a) and (b) are answered affirmatively, should the wife's separate assets have been included in the husband's net worth increase computation?

(d) If (a) and (b) are answered affirmatively, does the term "total amount of the deficiency" in section 293 (b) of the 1939 revenue code constitute an exception to or broadening of the term "deficiency" which section 271 (a) of that code applies to the entire chapter on income tax?

Petitioners contend that all of the above questions should be answered in the negative.

IV. STATUTES AND RULE INVOLVED

5. *26 USC sec. 7482—Courts of Review:*

"(a) Juridiction.—The United States Courts of Appeals shall have exclusive jurisdiction to review the decisions of the Tax Court."

6. *Sec. 272 of 1939 Revenue Code:*

"(a) (1) Petition to Board of Tax Appeals.—If in the case of any taxpayer, the Commissioner determines that there is a deficiency in respect of the tax imposed by this chapter, the Commissioner is authorized to send notice of such deficiency in tax to the taxpayer by registered mail. Within ninety days after such notice is mailed, the taxpayer may file a petition with the Board of Tax Appeals for a redetermination of the deficiency." (The name of said Board was changed to The Tax Court of the United States. Sec. 7441 of 1954 Revenue Code.)

7. *Rule 7 of the Tax Court*—Proper parties:

The proceeding shall be brought by and in the name of the person against whom the Commissioner determined the deficiency."

8. *Sec. 293 of 1939 Revenue Code:*

"(b) Fraud—If any part of any deficiency is due to fraud with intent to evade tax, then 50 per centum of the total amount of the deficiency (in addition to to such deficiency) shall be so assessed, collected and paid."

9. *Sec. 271 of 1939 Revenue Code—Definition of deficiency:*

"(a) In general.—As used in this chapter in respect of a tax imposed by this chapter, 'deficiency' means the amount by which the tax imposed by this chapter exceeds the excess of—

(1) the sum of (A) the amount shown as the tax by the taxpayer upon his return, plus (B) the amounts previously assessed (or collected without assessment) as a deficiency, over—(2) the amount of rebates."

V. STATEMENT OF THE CASE

10. Romm filed individual tax returns for 1942 through 1946. The deficiency notice was issued to Romm and his wife as joinly and severally liable. Both joined in the petition to the Tax Court under its Rule 6, *supra*, she appearing specially. The first issue raised in the petition was the erroneous joinder of the two parties in the statutory notice—no joint returns having been filed. At the trial, the Commissioner conceded this error and that the wife was not jointly and severally liable. The Tax Court made no jurisdictional ruling then or in its opinion, but issued both opinion and decision against the husband and wife jointly. Judge Sobeloff, for the Court of Appeals, ruled (Rec. p. 53) that the Tax Court undoubtedly committed an error which must be corrected but that it was not precluded from exercising jurisdiction. The mandate ordered modification of the decision without specific directions how the modification should be made.

11. The case arose on a net worth increase computation which included savings bonds and accounts owned by the wife individually, the increases therein being savings of the wife from Romm's $100 weekly household allowance to her. Petitioners so proved, the $5200 already having been included in the computation. The Tax Court held the increases nevertheless should be taxed because due to the husband's income and that petitioners had not supported their burden. The Court of Appeals affirms this double taxation. Record p. 56.

12. Prior to the deficiency notice, Romm voluntarily paid $16,436.79 (with interest) as a deficiency for 1946. The Commissioner assessed this deficiency but did not then assess a fraud penalty thereon. The Tax Court approved a 50 per cent penalty upon this $16,436.79 and the Court of Appeals affirmed it.

VI. REASONS RELIED UPON FOR ALLOWANCE OF THE WRIT

13. The Court of Appeals has rendered a decision contrary to the decision of this Honorable Court in *Hulburd* v. *Commissioner*, 56 S. Ct. 197; 296 US 306; 80 LEd 242. It also is in conflict with the decision of the Court of Appeals for the Second Circuit in *Bendheim* v. *Commissioner*, 214 F. 2 26. Involved are important questions of federal law which have not been but should be settled by this Honorable Court, including such a departure from the accepted and usual course of judicial proceedings as to call for an exercise of this Honorable Court's supervision.

(a) ***The Tax Court was without jurisdiction:***

14. The first issue raised below was whether the Tax Court had jurisdiction where the deficiency notice erroneously named the husband and wife as jointly and severally liable. The Commissioner conceded the error in the notice and that the wife was not so liable. The Tax Court not only then failed to make a bench ruling, but made no mention of the issue in either its opinion or decision, both of which were issued against both of the parties. Before the Court of Appeals, this jurisdictional issue was the first raised, also whether the complete failure to make any decision was in itself reversable error. The latter court held (Rec. p. 53) there undoubtedly was error which would have to be corrected, but that it was not prejudicial to the husband, therefore did not preclude the Tax Court from exercising jurisdiction. It remanded the case to the Tax Court for modification as to the liability of the wife. Record p. 63.

15. A valid deficiency notice is the formal and indispensable statutory premise to giving the Tax Court jurisdiction. Sec. 272 (a) (1) of the 1939 Code. Historically, if the notice goes to the wrong person, even at the cor-

rect address, to the proper person in the wrong legal status or by regular instead of registered mail, the decisions are that the Commissioner has not "determined a deficiency" which would give the Tax Court jurisdiction. *Leesa Dombrosky* v. *Comm.*, 35 BTA 1028; *Greve* v. *Comm.*, 37 BTA 450; *Gebelein* v. *Comm.*, 37 BTA 605; *Block* v. *Comm.*, 2 TC 761; and *Edith Stokby* v. *Comm.*, 26 TC ——, No. 114 (1956), the last-named holding that where, as here, no joint returns were filed, husband and wife must be considered separate taxpayers. The Commissioner conceded Mrs. Romm was not a taxpayer.

16. In *Hulburd* v. *Commissioner of Internal Revenue, supra,* the late Mr. Justice Cardozo, speaking for this Honorable Court, reversed the Seventh Circuit which had upheld a notice sent to the wrong person. He held that by statute the duty was upon the Commissioner to inquire and determine the proper person and not upon the then Board to revise his determination; that these were restraints upon jurisdiction which were binding not only upon the Board but upon the court of appeals with greater emphasis in reviewing the Board's action; that the adjudication there was made in seeming forgetfulness of the jurisdictional restrictions and to ignore them was error. Headnotes 1 and 2.

17. In *Bendheim* v. *Comm., supra,* the Court of Appeals for the Second Circuit held a Commissioner's "oversight" rendered the notice invalid and that it saw no reason in holding the Tax Court must assert jurisdiction upon the basis of the mistake. (p. 28) It refused to do precisely what the Fourth Circuit here has done. If the notice is invalid, everything based thereon is invalid.

18. The decision below excuses the Tax Court's undoubted error first on the ground it was "inadvertent" and second that the taxpayer (Romm) was not prejudiced since the notice asserted liability against him individually.

Two separate opportunities were given the Tax Court to decide the issue—first when the concession of error was made at the trial, and second when the issue was presented fully in petitioners' brief following trial. This cannot support inadvertence and inadvertence is no excuse where jurisdiction is involved. The assertion was of joint and several liability and the opinion and decision both were so issued by the Tax Court. Mrs. Romm at the conclusion still was not only held but, by a like avoidance rather than inadvertence, as shown below, her own assets still are approved by both courts as includable in the final tax computation. As to whether a taxpayer is "prejudiced" by errors as to parties in deficency notices, the Tax Court itself in numerous instances has dismissed, for want of jurisdiction, proceedings in which it appeared from the pleadings or record that there was a variance between the petitioners there and the taxpayers against whom the assertion was made. *J. F. McKean* v. *Comm.*, 15 BTA 795, citing *Bisso Ferry Co.* v. *Comm.*, 8 BTA 1104; *Bond, Inc.* v. *Comm.*, 12 BTA 339; *American Arch. Co.* v. *Comm.*, 13 BTA 552; *Sanborn Bros.* v. *Comm.*, 14 BTA 1059; and *Engineers Oil Co.* v. *Comm.*, 14 BTA 1148. In *McKean* both the Commissioner and the taxpayer asserted the Board did have jurisdiction and, if there was prejudice, it was waived. The decision below here is that in spite of the errors of both the Commissioner and the Tax Court, only one person should have been a party and is liable.

(b) ***Departure from Accepted Judicial Procedure:***

19. The function of a court of appeals is to determine whether the lower court has erred in law. Here the court of appeals found undoubted error. Record p. 53. Our issue was not, as it states, whether the Tax Court should limit liability to the husband, but that the deficiency notice was invalid, which and under the decisions deprived the Tax Court of jurisdiction. We also argued that,

apart from this, the failure of the Tax Court to make any ruling on the issue in itself was reversable error.

20. While a court of appeals may rule whether jurisdiction existed, it cannot, after finding error, excuse it and in effect confer jurisdiction. This would be what Mr. Justice Cardozo termed an assumption of power to change parties. *Hulburd, supra.* It is in this that petitioners contend the Court of Appeals has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Honorable Court's supervision and correction.

(c) *Inclusion of the wife's separate assets as taxable:*

21. There was no "inference", as stated by Judge Sobeloff (Record p. 65) that increases in the wife's own assets stemmed from the husband's household allowance. It was the uncontradicted evidence. Both the Commissioner and the Tax Court based their inclusion upon the fact her funds were attributable to the husband. Petitioners also pointed to the fact that such funds from the husband already were in the computation. Nowhere did the Commissioner meet this by showing that the wife had received any substantial funds from the husband in excess of the $5200 per year, as was called for under his burden. But the Tax Court held petitioners had not sustained their burden, even as to double taxation, and the court of appeals affirmed on the same ground. Mr. Chief Justice Taft, in *U.S.* v. *Supplee-Biddle Hdw. Co.*, 44 S. Ct. 546; 265 US 189, 196; 68 L.Ed. 970, 975, said that double taxation is to be avoided unless required by express words (of the statute).

22. Not only the wife's separate assets here are being taxed and doubly, but a 50 per cent penalty thereon is to be added under these decisions below. The zeal exhibited here, in thrice taxing the same income, merited a worthier cause—to paraphrase Circuit Judge Kalodner in *McCord* v. *Granger, Collector,* 201 F.2 103 at 108.

(d) *Sec. 293 (b) of the Code does not broaden sec. 271 (a) thereof:*

23. This issue never has been decided by this Honorable Court and, except for the present decision below, has been decided by only one court of appeals, which found there was confusion. *Middleton* v. *Comm.*, (CA-5) 200 F.2 94. There are no other authorities except Tax Court and Board decisions.

24. When the $16,436.70 deficiency for 1946 was assessed and paid prior to the deficiency notice, the Commissioner did not assess any 50 per cent penalty thereon. The notice recognized it as payment of tax only. Here again the Commissioner made a mistake if he intended to collect a penalty and here again both courts below resort to an unlegal statutory misconstruction to justify a clear extension beyond plain statutory phraseology—again to cover the Commissioner's failure to assess the penalty when he assessed the then deficiency. Once he failed therein, he knew, and both courts below know, that that $16,436.70 could not again be assessed. If the entire amount then claimed by the Commissioner then had been paid, it is untenable that either he or the courts could assess a penalty thereon where no deficiency was due. *Still* v. *Comm.*, 19 TC 1072, was the Tax Court's only cited authority. While this decision was affirmed in 218 F.2 639, the particular issue was not before the court of appeals. But our court below also cites *Still* and adds *Middleton, supra.*

25. Section 271 (a) specifies that the definition of "deficiency" therein contained shall apply to the entire chapter on income tax and under it the $16,436.70 plainly is to be excluded. But section 293 (b) states the fraud penalty shall be 50 per cent of the "total amount of the deficiency". This, *Middleton* holds, is well calculated to cause confusion, that 271 (a) relates to the unpaid portion of the tax but that it could well be said that 293 (b)

contemplates more than one deficiency—something which cannot legally happen as to any one year. Judge Sobeloff and *Middleton* theorize that a taxpayer may not avoid the penalty by paying a part of the Commissioner's informal claim, which they feel shows the "fallacy" of petitioners' argument. This prepayment was an entirely legal act, received on assessment as such. It is fundamental that any taxpayer may properly perform any legal act to reduce or minimize his liability.

26. This statutory confusion issue has recently (July, 1957) been answered by the Third Circuit in *Schwartzkopf* v. *Comm.*, 244 F.2 —— to the effect that if Congress meant to make one section an exception to or broadening of a conflicting section it should so have provided. The Commissioner for years has had abundant opportunity before Congress.

VII. CONCLUSION

27. It is submitted respectfully that the decision of the United States Court of Appeals for the Fourth Judicial Circuit should be reviewed and reversed and that, to such end, a writ of certiorari should be granted.

WARREN W. GRIMES
Shoreham Building,
Washington (5), D. C.,
Counsel for Petitioners.

Of Counsel:
HORACE J. DONNELLY, JR.,
640 Shoreham Building,
Washington (5), D. C.

UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

No. 7366.

Joseph N. Romm and Helen K. Romm, his wife,
Petitioners,

versus

Commissioner of Internal Revenue,
Respondent.

ON PETITION TO REVIEW THE DECISION OF THE TAX COURT OF THE UNITED STATES.

(Argued March 14, 1957. Decided May 27, 1957.)

Before SOPER and SOBELOFF, Circuit Judges, and HUTCHESON, District Judge.

Warren W. Grimes for Petitioners, and Arthur J. Gould, Attorney, Department of Justice, (Charles K. Rice, Assistant Attorney General and I. Henry Kutz, Attorney, Department of Justice, on brief) for Respondent.

SOBELOFF, Circuit Judge:

This is a petition to review the decision of the Tax Court holding the petitioner liable for income tax deficiencies and fraud penalties for the years 1942-46.

The year 1946 is open for deficiency assessment by the taxpayer's waiver of limitations, but the years 1942-45 are closed by limitations, unless the taxpayer filed fraud-

ulent returns with the intent to evade taxes in those years. Internal Revenue Code of 1939, Section 276 (a), 26 U. S. C. (1952 ed.) Section 276(a). The Tax Court found that the returns for those years were fraudulent and not closed to assessment.

Deficiencies were found for all five years, and the Tax Court concluded that as part of the deficiency in each year was due to fraud, the taxpayer was liable for the 50% penalty on the entire deficiency of each year as provided by the Internal Revenue Code of 1939, Section 293 (b), 26 U. S. C. (1952 ed.) Section 293 (b). Part of the deficiency for 1946 had already been paid, but the Court imposed the penalty on that amount as well as on the sum still due. The amounts of deficiency and penalty found to be owing are set out below.

Year	Income Tax	Additions to the Tax
1942	$2,159.56	$1,079.78
1943	2,145.22	1,072.61
1944	15,745.65	7,872.83
1945	16,853.67	8,426.84
1946	4,445.69	12,065.43

I.

The petitioner advances the contention that because no joint returns were ever filed, and only Joseph Romm filed individual returns, the Tax Court erred in holding Joseph Romm and his wife, Helen, jointly and severally liable for the deficiencies and penalties. The deficiency notice named them as jointly and severally liable and the petition for review by the Tax Court was brought in both names, in accord with the rules, but the Commissioner conceded, in the Tax Court and here, that the husband alone is liable. Taxpayer urges that the Tax Court was without juridiction, or, in any event, committed reversible error in not limiting liability to the husband. The

contention is unsubstantial. While the Court undoubtedly committed an inadvertent error, which must be corrected, it was not prejudicial to taxpayer. Inasmuch as the deficiency notice contained an assertion of liability against Joseph individually, the Tax Court was not precluded from exercising jurisdiction. Accordingly, the case will be disposed of on the merits.

II.

For many years, the petitioner, Joseph N. Romm, has been engaged in the retail sporting goods and bicycle servicing and repair business in Washington, D. C., trading under the name of Mount Vernon Cycle and Sports Shop, a sole proprietorship. He also operated a public bicycle concession in Potomac Park, and another bicycle rental business known as the Riverside Bicycle Academy, which was under the sole management of Harold Smith, and later James Butler. These men ran the Academy under an agreement that Romm would supply the bicycles, and that the profits would be distributed on a 70-30 basis after expenses; 70% going to Romm and 30% to the manager. It was stipulated that Romm also received substantial income from rental property during the years 1943-46.

In determining the deficiency, the Commissioner utilized the net worth method of reconstructing petitioner's income in the questioned tax years. The computation revealed taxpayer's yearly increase in net worth, and to this sum was added $5,200 annual living expenses and the federal taxes previously paid. The total for each yea was determined by the Commissioner to represent petitioner's taxable income for that year.

If certain disputed assets in the name of taxpayer's wife, Helen K. Romm, are omitted, the net worth analysis, as found by the Tax Court, shows the following as the

taxpayer's net income as compared with the income reported:

Year	Computed Income	Reported Income
1942	$12,052.20	$6,206.98
1943	10,435.00	6,195.30
1944	34,635.77	6,044.41
1945	36,529.00	7,523.40
1946	54,553.62	11,655.92

Taxpayer agrees that the government was justified in using the net worth method of determining income. For the most part he does not dispute the mathematical correctness of the computations, nor does he challenge the amounts for the various items. The only issue raised as to the net worth computation and the deficiency determined therefrom, is whether certain assets in the name of the wife should be included in the husband's net worth. It is the Commissioner's theory that these assets, consisting of U. S. Savings Bonds and several saving accounts, are attributable to the taxpayer's income and should be included. This the taxpayer contests.

Mrs. Romm came to this country in 1914, with $4,000. She married the taxpayer in 1916 and continued to work until 1921, earning six to eight dollars per week. At the end of 1941, she had assets totalling $2,258.95. The Commissioner determined that this amount represented the remainder of the original $4,000., augmented by her earnings. The taxpayer had gone through bankruptcy in the early 1930's, and from 1932 to 1941 had either filed no tax returns or reported little income. Nevertheless, in 1934 he had purchased a residence for $4,750. In light of these facts, the Tax Court concluded that inroads had been made on the wife's savings, and agreed with the Commissioner that Mrs. Romm's assets at the end of 1941, amounting to $2,258.95, correctly represented what

was left of her savings. Her year-end balances thereafter increased, and at the end of 1946 totalled $9,066.94.

The Tax Court held that with the exception of one savings account (found to represent independent savings of a daughter), and part of the proceeds of a $1,000. insurance policy (purchased by Mrs. Romm in 1924 and redeemed in 1944), the increases in her year-end balances were derived from the taxpayer's income, and should be included in the net worth computation of tax deficiencies.

In opposing the inclusion of these funds, taxpayer points to testimony by the wife and daughter that Mrs. Romm hoarded cash for many years; that she saved large sums from earlier earnings and also from the weekly allowances given her by Romm for the household expenses. The two inferences which the Tax Court was invited to draw are, first, that she had more than $2,258. at the beginning of the tax period, and second, that increases in her accumulated funds during the tax period stemmed from the household allowance made her by her husband for the family living expenses which amounts had already been included in the net worth analysis. This testimony, however, did not dissuade the Tax Court from upholding the Commissioner's inclusion of these assets in determining taxpayer's income and tax delinquency. The burden was on the taxpayer to overcome the Commissioner's determination, and we think the Tax Court not incorrect in holding that the taxpayer did not sustain his burden.

This testimony of the wife contained much inconsistency. At first she said she did not work after her marriage in 1921. Later, when government counsel sought to elicit testimony that her savings were invaded for the family living expenses in the 1930's she testified that she did work at the time to "help out." Still later, apparently hoping to fortify the claim that she had accumu-

lated large savings in the 1930's, she again contradicted herself by saying that she saved everything which she earned in those years. Palpably, there is no reconcilila-tion of these three versions—that she didn't work, that she worked and contributed to the family's support, and that she worked and retained all of her earnings. Considering the character of the evidence which was unconvincing to the Tax Court, we cannot say the findings below were clearly erroneous.

It is also contended that a $2,000. loan from Mrs. Romm to her husband in 1946 should have been deducted from petitioner's net worth. There is no merit in this contention, because if the money is regarded as Mrs. Romm's, it would nevertheless be includable in the taxpayer's net worth computation since, if it had not been loaned, her year-end balance for 1946 would have been $2,000.00 higher. This additional $2,000.00 would have been includable in the husband's net worth analysis along with the balance hereinbefore discussed.

The next major issue raised in the petition relates to the finding of fraud. Upon this issue depends the assessability of the deficiencies for 1942-45—which are otherwise barred by limitations—and the fifty percent penalty for those years and 1946 as well. The question being basically factual, our inquiry is whether or not the Tax Court's decision is clearly erroneous. Title 26 U.S.C.A. Sec. 7482. See *Commissioner* v. *Smith Paper* 1 Cir., 222 F. 2d 126, 128; *Farnsworth* v. *Commissioner*, 5 Cir., 203 F. 2d 490.

In our judgment, the finding of fraud is amply supported. For five consecutive years there was a gross discrepancy between income earned and income reported, the income earned being, at times, approximately four hundred percent higher.

While a consistent pattern of large understatements of income may not alone be sufficient to sustain the Government's proof of fraud, it is a strong circumstance when accompanied by other indicia of willfulness. *Holland* v. *United States*, 348 U. S. 121; *Beard* v. *United States*, 4 Cir., 222 F. 2d 84; *Lipsitz* v. *Commissioner*, 4 Cir., 220 F. 2d 871; *Rogers* v. *Commissioner of Internal Revenue*, 6 Cir., 111 F. 2d 987. Here the evidence indicates that the taxpayer knew of the disparity, and the Tax Court was so persuaded. We cannot say that this evaluation of the evidence, and the inference therefrom of fraudulent intent, is patently erroneous.

The taxpayer's knowledge of the disparity is readily inferrable from several circumstances. Between November 7, 1941, shortly before the beginning of the tax years involved, and December 31, 1946, the end of the period, the petitioner submitted five net worth statements to the City Bank of Washington for credit purposes, and he discussed them with the bank president. Each successive statement showed a marked increase in the petitioner's net worth, far in excess of the income reported, even if the real estate included in the statements is reduced from its market value to cost as was done in the Tax Court. As the Commissioner points out, the total growth in net worth revealed by these credit statements, when the realty is reduced from market to cost, is $161,762.19, while the income reported was merely $37,626.01.

Though we are referred to testimony of the bank president that Romm did not have a clear understanding of certain accounting details, the evidence indicates that he understood the total figures in the statements and their significant bearing on his financial status. Despite this awareness, he, for five years, signed tax returns reporting far less. Petitioner sought to show that he had no understanding of the returns, and that he merely signed whatever his bookkeeper McMillan put before him. The

record discloses, however, that though the computations from the books were done by McMillan, Romm nevertheless had a part in preparing the returns. Not only did he supply detailed itemized figures of personal deductions to be claimed, but also McMillan himself testified that Romm knew the contents of the returns, and that the two of them discussed the income reported and the amount of the tax.

Significant also is other evidence of prosperity. The taxpayer paid off a mortgage of $26,500. between 1943 and 1946, bought a new summer home at Ocean City, Maryland, for $19,000. more than he received for the old home, and advanced his wife $26,000. for their household expenses over the five years. These three major expenditures, of which he obviously knew, alone represented over $71,000. that passed through his hands during these five years; and yet he reported only $37,626.01 income for the same period. Moreover, in connection with the mortgage referred to there was revealed a circumstance, frequently present in tax fraud cases, which is not unmeaningful here. It was shown at the trial that of the thirty-one payments on this mortgage between 1943 and 1946, only thirteen were made by check. A permissible inference is that the remaining eighteen, paid in cash, came from hidden funds. While it would not necessarily follow that these sources, if untaxed, had been accumulated from 1942-46 income, the practice has relevant bearing on the taxpayer's intentions and general state of mind.

Beyond this abundance no more evidence is needed. But there is more. The Tax Court thought it significant, as do we, that Romm did not, in the years in question, report any income whatever from the Riverside Bicycle Academy. As previously noted, this rental business was under the sole management of other individuals who paid current expenses out of receipts. Each week the gross receipts were turned over to Romm, and at the end of the

season in October it was divided on a 70-30 basis, 70% going to Romm. From the records introduced in evidence, it was clear that Romm's share of the net profits, after deducting the cost of rent for the season (Spring to October) was $4,707.27 in 1943, $1,882.91 in 1944, $2,359.70 in 1945, and approximately $2,000. in 1942 and 1946 each. Undeniably, petitioner knew he was receiving income from this source. A revenue agent testified that Romm had told him he realized almost $2000 per year from the operation. Nevertheless, no income from the Academy was ever reported.

Taxpayer offers several explanations for the omission. One is that the rent for the off-season and the cost of the bicycles were paid by himself after the net receipts were divided. The plain answer is that the off-season rent alone was too negligible to wipe out his profits, and the only tax year in which bicycles were bought was 1946, and this would not explain the failure to report income in the four previous years.

It was also asserted by taxpayer that he and his manager had an agreement that the latter would pay taxes. This the manager denied, and even beyond the question of veracity, the Tax Court was not required to accept it as an adequate explanation.

All this evidence, which fully supports the inference of fraud, taxpayer sought to overcome by testimony that he was incompetent with figures and books and relied entirely on his bookkeeper, McMillan, to make his tax returns. And it was also suggested that McMillan himself was incompetent in these matters.

This evidence the Court was not obliged to believe as it depended in large part upon the credibility of the witnesses. Moreover, this evidence does not meet the issue squarerly. The government was not attempting to prove that there was falsification merely in transferring figures from the books. The theory of its case was not so re-

stricted. The inference they sought to sustain is that somewhere along the line, from actual sales in the petitioner's stores to the filing of the tax returns, substantial sums of income were knowingly and intentionally concealed by taxpayer—in short, that he knew that he had earned more than he reported.

This theory, well grounded in the evidence, is not negatived by suggestions of taxpayer's good faith based on his failure to claim certain deductions which he might have claimed. Testimony by members of Romm's family, that the home at Ocean City was used to entertain business guests, was of a self-serving nature. Like the testimony regarding McMillan's responsibility for the returns and his incompetence, it weight depended on nebulous and subtle factors of credibility perceptible to the fact-finder, before whom the living witnesses appeared, but not readily gleaned from the record on appeal. The additional point that taxpayer could have, but did not, claim depreciation for the bicycles used at the Academy is without merit. Though depreciation was not expressly set out in the schedules provided in the returns, the bookkeeper, McMillan, testified that from 1942 to 1945 the bicycles were written off on a two year basis on information obtained from the Bureau of Internal Revenue. Hence, taxpayer got the benefit of depreciation, apparently charging it off to costs not readily discoverable in an examination of the tax returns.

IV.

Another argument advanced by the petitioner is equally lacking in substance. It is said that the fraud penalty should not be levied upon the portion of the 1946 deficiency which had been voluntarily paid before the deficiency notice was delivered. Before the deficiency notice was sent, taxpayer paid $24,572.04, of which $16,436.79 was credited to the deficiency, $7,303.41 to interest, and $831.24 was designated as a 5% negligence penalty.

Taxpayer contends that the "deficiency" upon which the fraud penalty is levied by Section 293 (b) is determined by the definition of "deficiency" contained in Section 271 (a). In general terms, the definition of Section 271 (a) is that a deficiency is the amount by which the total tax liability exceeds the total of all amounts previously paid. We do not think that the word "deficiency" in Section 293 (b) was meant to be so restricted. We agreed with the Commissioner that it means the original deficiency in its entirety, as was held in *Middleton* v. *Commissioner of Internal Revenue*, 5 Cir., 200 F. 2d 94. The fallacy of the construction proposed by taxpayer, and the folly of the result if his construction should be adopted, is made plain in the very facts before us. When the sum was paid by Romm, the investigation was already underway, as he had reason to know. By then paying the tax, he could not obliterate the consequences of the earlier fraud. As the Tax Court said in *Still, Inc.* v. *Commissioner*, 19 T. C. 1072, 1077, affirmed 2 Cir., 218 F. 2d 639, such a result would allow fraudulent taxpayers to "make sport of the so-called fraud penalty."

V.

We think, however, that in one respect the Tax Court committed error. When taxpayer paid part of the 1946 deficiency in advance of the deficiency notice, naturally no penalty of any kind had yet been assessed. No specific designation was made by the taxpayer or could have been made at that time as to the precise application of the fund; there was only one possible application, that is to say, to the deficiency. The Commisisoner, however, allocated $831.24 to penalty for negligence, and a part to interest. The rest was applied to the deficiency in taxes. Later, when the Commissioner decided to impose the much larger penalty for fraud, he cancelled the negligence penalty of $831.24. It was at this time that the Commissioner, without consulting the taxpayer, applied the

$831.24 to the fraud penalty rather than to the deficiency still owing. Taxpayer submits to us that this sum should have been credited to the tax deficiency, and we agree. When the assertion of negligence was discarded, the taxpayer technically became entitled to the $831.24. If the money had been repaid to him, he would have had the option to designate the application of the fund to deficiency, which would have stopped interest on that amount. The taxpayer was not afforded this option, since the Commissioner undertook to decide the question for him. The result was that the interest continued running on the $831.24. There is no fair reason in principle or authority, why the taxpayer should be held liable for an accumulation of interest on a sum of money already paid.

The case is remanded to the Tax Court for modification of the order as to interest on the deficiency and as to the liability of taxpayer's wife. In all other respects, the decision is affirmed.

Affirmed and remanded for modifications.

Tax Court Opinion

MEMORANDUM FINDINGS OF FACT AND OPINION

The respondent determined deficiencies in income taxes and penalties for the years 1942 to 1946, inclusive, as follows:

Year	Deficiency	50 Per Cent Addition to Tax
1942	$2,159.56	$1,079.78
1943	2,211.52	1,105.76
1944	16,321.23	8,160.61
1945	17,098.79	8,549.39
1946	9,582.49	12,187.80

Filed and Entered May 27, 1957

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 7366

Joseph N. Romm and Helen K. Romm, his wife,
Petitioners,

v.

Commissioner of Internal Revenue,
Respondent.

JUDGMENT

ON PETITION to Review the Decision of The Tax Court of the United States.

THIS CAUSE came on to be heard on the transcript of the record from The Tax Court of the United States, and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the decision of the said The Tax Court of the United States, in this cause, be, and the same is hereby, modified as set forth in the opinion of the Court filed herein and, as so modified, it is affirmed; and that this cause be, and the same is hereby, remanded to The Tax Court of the United States for further proceedings not inconsistent with the opinion of the Court filed herein. May 27, 1957.

SIMON E. SOBELOFF
United States Circuit Judge.

June 29, 1957, mandate issued and transmitted to the Clerk of The Tax Court of the United States at Washington, D. C.

The issues are (1) whether any part of the deficiencies for the several years was due to fraud with the intent to evade tax within the meaning of section 293 (b) of the 1939 Internal Revenue Code; (2) whether certain United States savings bonds and year-end balances in the name of Helen K. Romm were properly included in the net worth analysis of Joseph N. Romm; (3) whether the statute of limitations bars the assessment of deficiencies for the years 1942 to 1945, inclusive; (4) whether the amount of $821.84 voluntarily paid in 1954 by Joseph N. Romm as a "negligence penalty" to apply to the year 1946 should be credited to the deficiency computed for that year or whether it should be credited to the 50 per cent addition for fraud determined by the respondent for 1946; and (5) whether the 50 per cent addition for fraud for 1946 should be based on the deficiency as determined for that year before crediting such deficiency with the voluntary payment, in the amount of $16,436.79, made by Joseph N. Romm in 1954 to apply to the year 1946.

Findings of Fact.

Some of the facts have been stipulated and they are found accordingly.

Joseph N. and Helen K. Romm, husband and wife, were residents of Takoma Park, Maryland. Joseph N. Romm (hereinafter called the "petitioner") filed separate individual income tax returns for years 1942 to 1946, inclusive, with the then collector of internal revenue at Baltimore, Maryland. Petitioner's wife, Helen, filed no returns for any of the years involved.

Petitioner was in the business of selling merchandise, prineipally sporting goods, at retail in the Washington metropolitan area under the trade name of Mt. Vernon Cycle and Sport Shop, a sole proprietorship. Bicycle repair and service facilities were also provided at the stores operated by the petitioner. From 1935 to 1948,

petitioner operated a public bicycle concession in Potomac Park under contract with the National Park Service. Petitioner also had an interest during the years here involved in the Riverside Bicycle Academy (hereinafter called the "Academy"), a bicycle rental business for which he furnished the bicycles and other equipment. The Academy was managed by Harold E. Smith, who was replaced by James Butler for a period when Smith was in the Armed Forces. Weekly receipts during the rental season (from April to October) were turned over to petitioner or one of his employees with a written statement of the week's operations. Smith received no compensation until the end of the season when 30 per cent of the net profits were paid to him, the balance going to the petitioner. Net profits were determined by subtracting from gross receipts all expenses of the Academy, including the cost of repair parts and the rent for the Academy paid by the petitioner during the winter months. Depreciation for the bicycles was taken by petitioner in his return. Petitioner did not report any of the income from the Academy in his returns for the years 1942 to 1946, inclusive. Net profits in 1943 from the Academy amounted to $6,724.67, of which Smith's share was $2,017.40, and the balance of $4,707.27 going to the petitioner. In 1944 Smith's share of the net profits was $806.96, indicating that the petitioner received $1,882.91. In 1945 the net profit from the Academy was $3,371, of which 30 per cent was $1,011.30 ($404.52 paid to Smith and $606.78 paid to Butler), leaving $2,359.70 for the petitioner. Similarly, the petitioner received his portion of the net profits in 1942 and 1946 from the operations of the Academy. Petitioner received as his share of the net profits in each of these two years approximately $2,000. Petitioner reported no income on his returns for 1942 to 1946, inclusive, from the operations of the Academy.

During the years 1943 to 1946, inclusive, petitioner received substantial income from rental property.

From 1943 until after the end of 1946 the petitioner's accounts were kept by Robert S. McMillan. Up to July 1946, McMillan worked on a part time basis, mostly at night, and from July 1946 he worked a full time basis, being in charge of the books, records, and office work, and occasionally helping in sales and in taking inventory.

The parties agree it was appropriate for the respondent to use the net worth plus personal living expenses method to determine the petitioner's net income for the years 1942 to 1946, inclusive. It was also stipulated that all of the amounts used in the net worth analysis were correct. Petitioner contended the wife's assets should not be included but stipulated the amounts of said assets were correct. The wife's assets, as stipulated, were:

	December 31					
	1941	1942	1943	1944	1945	1946
U. S. Savings Bonds	$ 712.50	$2,537.50	$3,287 50	$4,075.00	$4,562.50	$4,[illegible]50
Suburban Bank	339.30	127.10	208.75	252.46	476.38	648.67
Columbia Federal Sav. & Loan Ass'n.	159.50	23.38	199.57	1,500.90	1,787.10	2,241.41
National Permanent Building & Loan Ass'n. (No. R-592)	488.06	459.06	1,236.21	303.26	315.46	327.37
National Permanent Building & Loan Ass'n. (No. R-714)			161.70	508.05	868.50	1,211.99
Lincoln National Bank	559.59	5.45				
Totals	$2,258.95	$3,152.49	$5,093.73	$6,639.67	$8,009.94	$9,066.94

The net worth analysis, as stipulated, omitting the above assets, was as follows:

Assets	December 31 1941	1942	1943	1944	1945	1946
City Bank—Mt. Vernon acc't.	$ 8,215.27	$13,064.49	$ 6,033.12	$ 25,556.88	$ 41,607.82	$ 53,390.98
Columbia Fed. Sav. & Loan Ass'n. acc't.						811.42
City Bank—Gus Romm acc't.	8.32	1,193.61	3,061.44	1,494.01	1,879.38	159.47
Automobile	1,480.00	1,480.00	1,480.00	1,480.00	1,480.00	1,480.00
U. S. Savings Bonds		1,325.00	3,500.00	3,500.00	3,500.00	3,500.00
Bank of Ocean City—special	39.30	39.30				549.75
Bank of Ocean City—regular	151.98	172.96	1,776.61	777.29	2,053.96	316.72
6613 Eastern Avenue	4,750.00	4,750.00	4,750.00	4,750.00	4,750.00	4,750.00
6617 Eastern Avenue		3,700.00	3,700.00	3,700.00	3,700.00	3,700.00
933 G Street			45,000.00	45,000.00	45,000.00	45,000.00
5019 Wisconsin Avenue				15,000.00	15,000.00	15,000.00
924 G Place					10,000.00	10,000.00
Garage						6,779.21
Two Ocean City lots and summer home	8,000.00	8,000.00	8,000.00	8,000.00	8,000.00	
Another Ocean City lot	1,600.00	1,600.00	1,600.00	1,600.00	1,600.00	1,600.00
Another summer home						27,326.97
Furniture and Fixtures					401.50	401.50
Inventories	28,860.32	27,180.10	18,824.69	15,261.84	20,883.81	50,200.87
Bicycles (one lot)						2,519.00
Bicycles (another lot)	12,665.00	12,665.00	12,665.00	12,665.00	12,665.00	12,665.00
Equipment				867.00	867.00	867.00
City Bank—rental acc't.			482.92	714.09	3,578.48	1,122.19
Total assets	$65,770.13	$75,170.46	$110,873.78	$140,366.11	$176,966.95	$242,140.08

Liabilities	December 31 1941	1942	1943	1944	1945	1946
Reserve for depreciation	$13,035.00	$13,405.00	$13,938.39	$15,104.14	$15,940.04	$17,303.52
City Bank loan						7,070.78
Bank of Ocean City loans	500.00					1,000.00
City Bank—second loan					10,000.00	
City Bank—third loan						4,000.00
Mortgage on 933 G Street			26,591.67	17,482.45	4,993.47	
Mortgage on 5019 Wisconsin Ave.				8,968.10	7,683.61	6,346.75
Accounts payable		2,664.62	5,937.24	5,633.50	15,132.29	34,189.97
Total liabilities	$13,535.00	$16,069.62	$46,467.30	$47,188.19	$53,749.41	$69,911.02
Net worth	52,235.13	59,100.84	64,406.48	93,177.92	123,217.54	172,229.06
Less prior year's net worth		52,235.13	59,100.84	64,406.48	93,177.92	123,217.54
Increase in net worth		$ 6,865.71	$ 5,305.64	$28,771.44	$30,039.62	$49,011.52
Federal income tax paid		453.78	972.84	1,589.64	2,620.00	1,332.72
Household expenses		5,200.00	5,200.00	5,200.00	5,200.00	5,200.00
Less: Allowable deductions		(467.29)	(1,043.48)	(925.31)	(1,330.62)	(990.62)
Totals		$12,052.20	$10,435.00	$34,635.77	$36,529.00	$54,553.62

Petitioner's wife, Helen, brought with her $4,000 when she came to this country in 1914. She married the petitioner in 1916. From 1914 to 1921 she worked at various jobs, earning six to eight dollars per week. In the early thirties petitioner went through bankruptcy, and from 1932 through 1941 he filed no returns in some years and in others he paid small amounts of income tax. In 1934 the petitioner purchased a residence for himself and his wife, for $4,750. On December 31, 1941, the petitioner's wife had assets in the amount of $2,258.95. During the years 1942 to 1946, inclusive, she acquired with funds obtained from the petitioner U. S. savings bonds and accounts in several banks. An account in the National Permanent B. & L. Association (No. R-714), which was in the wife's name, represents savings of the petitioner's daughter.

The respondent was correct in using the wife's year-end balances for the years 1942 to 1946, inclusive, in determining petitioner's net worth for said years with the exception of the account in the National Permanent B. & L. Association (No. R-714), which account really belonged to their daughter.

On or about the dates set forth below, the petitioner submitted net worth statements to the City Bank of Washington, D. C. for credit purposes. The amounts of the net worth indicated on such statements were as follows:

Date	Net Worth
November 7, 1941	$41,341.83
October 31, 1942	41,341.83
January 1, 1944	60,054.56
September 26, 1945	166,565.24
December 31, 1946	266,697.84

In these statements submitted to the bank real estate was listed, in some instances, at estimated fair market

value, instead of cost. If the cost figures were used consistently in the net worth statements they would show the following net worth amounts and the increases in net worth in each year:

Date	Net Worth
November 7, 1941	$37,091.83
October 31, 1942	55,804.56
January 1, 1944	86,692.03
September 26, 1945	127,615.24
December 31, 1946	198,854.02

Petitioner aided McMillan, the bookkeeper, in the preparation of the net worth statements, applying estimates of the fair market value of various parcels of real estate owned by him. Petitioner discussed these statements with the president of the City Bank.

Petitioner reported the following amounts of net income in his returns filed for the years 1942 to 1946, inclusive:

1942	$6,206.98
1943	6,195.30
1944	6,044.41
1945	7,523.40
1946	11,655.92

The returns, prepared by McMillan from the books and records maintained by him, were prepared in detail, with deductions, expenses, and income items set out in odd amounts. The petitioner assisted McMillan in preparing the returns for each of the years here involved, and the petitioner was aware of the income reported in each of the annual returns.

On August 11, 1954, prior to the issuance of the deficiency notice, the petitioner made a payment of $24,572.04 to the district director of Internal Revenue at Bal-

timore, Maryland, to apply to the income tax for the year 1946. Or the receipt issued by the director's office $16,436.79 was shown as applicable toward a deficiency in income tax for 1946, $7,303.41 as interest, and $821.84 as a "5% penalty."

Petitioner sustained a net operating loss of $6,974.34 in 1948, and it has been conceded by the respondent that this amount is to be allowed as a carry-back to the year 1946. Effect shall be given to this adjustment in petitioner's income tax deficiency for 1946 in the Rule 50 computation.

A part of the deficiency in petitioner's income taxes for each of the years 1942 to 1946, inclusive, was due to fraud with intent to evade tax. In each of the years here involved, 1942 to 1946, inclusive, the petitioner filed fraudulent returns with the intent to evade tax.

Opinion.

Mulroney, *Judge:* The petitioner argues that the years 1942 to 1945, inclusive, are barred by the statute of limitations. Where a taxpayer files a false or fraudulent return with intent to evade tax a proceeding in court may be commenced at any time to collect whatever taxes are due. Section 276 (a) of the 1939 Internal Revenue Code. Respondent has determined the 50 per cent addition for fraud in addition to deficiencies in petitioner's income tax for the years 1942 to 1946, inclusive. Section 293 (b) of the 1939 Internal Revenue Code provides for a 50 per cent addition to the tax where any part of the deficiency of any year is due to fraud with intent to evade tax.

The respondent has the burden of proof on fraud and he must prove fraud in each instance by evidence which is clear and convincing. It was necessary for the respondent to compute unreported amounts of income in the years involved by the net worth plus personal living expendi-

tures method, and the petitioner agrees that this was justified in this case. However, petitioner does argue that the respondent was not justified in including in the net worth computations certain assets standing in the name of the petitioner's wife. We shall treat this issue later in the opinion. A comparison of the amounts of net income reported by the petitioner in his returns for the years involved and the amounts of net income as determined by the net worth analysis reveals substantial understatements. Petitioner reported net income of $6,206.98 in 1942, $6,195.30 in 1943, $6,044.41 in 1944, $7,523.40 in 1945, and $11,655.92 in 1946, while the net worth analysis (not including assets in the name of the petitioner's wife) shows net income for those years of $12,052.20, $10,435.00, $34,635.77, $36,529.00, and $54,553.62, respectively. Large understatements of income which appear consistently over a period of years are evidence of fraud. *M. D. Eagle, Jr.*, 15 T.C. No. 25 (filed October 31, 1955); *Arlette Coat Co.*, 14 T.C. 751. Petitioner was an experienced businessman who, in spite of his meager schooling, was able to build a substantial business over the years. He purchased several pieces of real estate in the years 1942 to 1945, and in 1946 he made substantial improvements to real estate owned by him and he also built a summer home at a cost of $27,326.97. Especially significant is the fact that a mortgage of $27,500, in connection with the purchase in 1943 of real estate at a cost of $45,000 was completely paid off by 1946. The evidence shows that a substantial portion of this was paid in cash, and the only apparent source of this cash was out of petitioner's business income. Petitioner maintained a checking account to be used primarily in his business, and the year-end balances in this account went from $8,215.21 on December 31, 1941, to $53,390.98 on December 31, 1946. This represented an increase of $45,175.77, and during the same period the petitioner reported net income of only $37,626.01. Evidence of the petitioner's awareness of the

marked increases in his net worth over these years appears in the net worth statements filed by him with a bank in establishing credit. There is a substantial difference between the net worth amounts submitted in these statements and the amounts of net income reported by the petitioner in the corresponding year. Petitioner discussed these statements with the bank officers and it is clear that he was well cognizant of the information contained in them. We do not believe that the petitioner was unaware that his actual income in each of the years involved was substantially greater than the amounts reported by him.

Petitioner received income from the Riverside Bicycle Academy during the years 1942 to 1946, inclusive, and none of this income was ever reported by him in his returns for those years. His explanation of these omissions was it had been agreed that the manager of the Academy, Smith, was to pay petitioner's tax on such income. Smith denied the existence of any such agreement. We do not believe that such an agreement existed and we consider the omissions in each of the years here involved as still another manifestation of fraudulent intent. Furthermore, the petitioner could not escape his duty to report his share of that income.

Petitioner offers no tenable explanation for his failure to report these substantial amounts of income in the years involved here. *Arlette Coat Co., supra.* Some of his explanations are vague and lack coherence. He attempts to blame faulty accounts kept by his bookkeeper for the discrepancies but we are wholly unpersuaded that the bookkeeping methods, though admittedly loose, explain the substantial gap between the income earned from petitioner's business and the income reported by him in each of the years before us. Moreover, the petitioner was intelligent enough to realize clearly that he was reporting only a fraction of the income properly reportable in each taxable year.

A careful examination of all the evidence and the record as a whole reveals in a clear and convincing manner that the petitioner deliberately omitted the large part of his income from his returns for each of the taxable years here involved. *M. D. Eagle, Jr., supra.* We hold that the returns filed by the petitioner for the years 1942 to 1945, inclusive, were fraudulent with intent to evade tax and consequently, under section 276 (a) of the 1939 Code, the statute of limitations does not bar assessment of tax for those years. We hold also that part of the deficiency for the years 1942 to 1946, inclusive, was due to fraud with intent to evade tax. The respondent included in the petitioner's net worth analysis certain assets held in the name of petitioner's wife. The argument for this is that such assets were acquired with income earned by the petitioner in his business operations during the years involved here. Petitioner contends that his wife had $4,000 before they were married in 1916, and that this fund, together with savings from meager wages from 1914 to 1921 and money received from her daughter and son-in-law, was the source of the assets in her name. However, there is evidence that petitioner went through a bankruptcy in the early 1930s, and it also appears that in several of the years, 1932 through 1942, he did not file returns or paid a small tax when returns were filed. Moreover, it appears that the petitioner purchased a residence in 1934 for $4,750. All this would indicate that inroads were made on any funds belonging to petitioner's wife over these years. On December 31, 1941, assets in the amount of $2,258.95 were in the name of the wife, and we believe this adequately covers whatever remained from the early years of the funds originating with her. We believe that the balances in the account in the wife's name at the National Permanent Building and Loan Association, number R-714, represent savings of petitioner's daughter and cannot be attributed to the petitioner. Nor do we believe that the proceeds of the

endowment policy deposited in the wife's account in 1944 should be attributed to the petitioner in their entirety. See Regulations 111, Sec. 29.22(b)(2)-1. With the exceptions noted, we are persuaded that the assets in the wife's name are attributable to income earned by the petitioner in the years involved here and should therefore be included in the net worth computations.

There is no merit in petitioner's argument that the 50 per cent addition for fraud cannot be applied to the entire deficiency for 1946 where a part of the tax had been paid prior to the deficiency notice. *George M. Still, Inc.*, 19 T.C. 1072, affd. per curiam, 218 F. 2d 639; *Arlette Coat Co., supra; Aaron Hirschman,* 12 T.C. 1223. We hold that the fraud addition should be computed upon the whole deficiency computed for 1946, without reducing such deficiency by the amount which was paid by the petitioner, voluntarily, toward his 1946 tax liability.

Petitioner apparently has abandoned his claim for a loss from a purported store robbery in 1946. There was no evidence introduced to discharge the petitioner's burden of proof on this point, and we hold that such loss is disallowed.

It has been stipulated that the petitioner sustained a net operating loss in 1948 of $6,974.34, and that such amount is to be allowed as a carry-back to 1946. Section 122 (b)(1) of the 1939 Internal Revenue Code. There is some indication in petitioner's brief that he is arguing the carry-back is to be used to reduce the deficiency in 1946 before the 50 per cent addition for fraud. There is no merit in this argument. The 50 per cent addition is to be added before any reduction on account of the carry-back. *Auerbach Shoe Co.*, 21 T.C. 191, affd. 216 F. 2d 693; *P.C. Petterson*, 19 T.C. 486; *Nick* v. *Dunlap*, 185 F. 2d 674, certiorari denied 341 U.S. 926.

Decision will be entered under Rule 50.

Decision

Pursuant to the Court's Memorandum Findings of Fact and Opinion filed April 30, 1956, the parties herein having filed an agreed computation of tax on July 24, 1956, it is

ORDERED and DECIDED: That there are deficiencies in income tax and additions to the tax, as follows:

Year	Income Tax	Additions to the Tax
1942	$2,159.56	$1,079.78
1943	2,145.22	1,072.61
1944	15,745.65	7,872.83
1945	16,853.67	8,426.84
1946	4,445.69	12,065.43

(Signed) LUTHER A. JOHNSON
Judge.

Entered July 26, 1956

Office - Supreme Court, U.S.
FILED
SEP 19 1957
JOHN T. FEY, Clerk

No. 389

In the Supreme Court of the United States

October Term, 1957

JOSEPH N. ROMM AND HELEN K. ROMM, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF FOR THE RESPONDENT IN OPPOSITION

J. LEE RANKIN,
Solicitor General,

CHARLES K. RICE,
Assistant Attorney General,

I. HENRY KUTZ,
MILDRED L. SEIDMAN,
Attorneys,
Department of Justice,
Washington 25, D. C.

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No. 389

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COMMISSIONER OF INTERNAL REVENUE

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BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Court of Appeals (Pet. 11-22) is not yet reported. The memorandum findings of fact and opinion of the Tax Court (Pet. 22-35) are not reported.

JURISDICTION

The judgment of the Court of Appeals (Pet. 22-A) was entered on May 27, 1957. The petition for a writ of certiorari was filed on August 20, 1957. The jurisdiction of this Court is invoked under 28 U.S.C. 1254.

QUESTIONS PRESENTED

1. Whether the Tax Court had jurisdiction to hear this case although the Commissioner's notice of deficiency was addressed to taxpayer [1] and his wife and subsequently the Commissioner conceded that taxpayer's wife is not liable for the deficiencies.

2. Whether the record warrants the Tax Court's determination, which was affirmed by the court below, that certain assets of taxpayer's wife were attributable to taxpayer's earnings and properly includible in his net worth analysis.

3. Whether the fraud penalty under Section 293(b) of the Internal Revenue Code of 1939 attaches to the original deficiency for 1946 in its entirety, unreduced by payments which were made shortly before the delivery of the deficiency notice.

STATUTE AND RULE INVOLVED

Internal Revenue Code of 1939:

SEC. 51 [2] [As amended by Sec. 11(a) of the Individual Income Tax Act of 1944, c. 210, 58 Stat. 231]. INDIVIDUAL RETURNS.

* * * *

(b) *Husband and Wife.*—A husband and wife may make a single return jointly. Such a return

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[1] Taxpayer, as used herein, refers to Joseph N. Romm only.

[2] The amendment by the Individual Income Tax Act of 1944 is effective for taxable years beginning after December 31, 1943. However, the section as applicable for the years 1942 and 1943 is substantially the same.

may be made even though one of the spouses has neither gross income nor deductions. If a joint return is made the tax shall be computed on the aggregate income and the liability with respect to the tax shall be joint and several. No joint return may be made if either the husband or wife is a nonresident alien or if the husband and wife have different taxable years. The status of individuals as husband and wife shall be determined as of the last day of the taxable year.

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(26 U.S.C. 51.)

SEC. 271 [As amended by Sec. 14 (a) of the Individual Income Tax Act of 1944, *supra*].

DEFINITION OF DEFICIENCY.

(a) *In General.*—As used in this chapter in respect of a tax imposed by this chapter, "deficiency" means the amount by which the tax imposed by this chapter exceeds the excess of—

(1) the sum of (A) the amount shown as the tax by the taxpayer upon his return, if a return was made by the taxpayer and an amount was shown as the tax by the taxpayer thereon, plus (B) the amounts previously assessed (or collected without assessment) as a deficiency, over—

(2) the amount of rebates, as defined in subsection (b) (2), made.

* * * *

(26 U.S.C. 271.)

SEC. 272. PROCEDURE IN GENERAL.

(a) (1) [As amended by Sec. 203 (a), Act of December 29, 1945, c. 652, 59 Stat. 669]. *Peti-*

tion to the Tax Court of the United States.—If in the case of any taxpayer, the Commissioner determines that there is a deficiency in respect of the tax imposed by this chapter, the Commissioner is authorized to send notice of such deficiency to the taxpayer by registered mail. Within ninety days after such notice is mailed (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the ninetieth day) the taxpayer may file a petition with the Tax Court for a redetermination of the deficiency. No assessment of a deficiency in respect of the tax imposed by this chapter and no distraint or proceeding in court for its collection shall be made, begun, or prosecuted until such notice has been mailed to the taxpayer, nor until the expiration of such ninety-day period, nor, if a petition has been filed with the Tax Court, until the decision of the Tax Court has become final.

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(26 U.S.C. 272.)

SEC. 293. ADDITIONS TO THE TAX IN CASE OF DEFICIENCY.

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(b) *Fraud.*—If any part of any deficiency is due to fraud with intent to evade tax, then 50 per centum of the total amount of the deficiency (in addition to such deficiency) shall be so assessed, collected, and paid, in lieu of the 50 per centum addition to the tax provided in section 3612 (d) (2).

(26 U.S.C. 293.)

Rules of Practice Before the Tax Court of the United States (Rev. August 15, 1955):

RULE 6. PROPER PARTIES.

The proceeding shall be brought by and in the name of the person against whom the Commissioner determined the deficiency [or liability, as the case may be], or by and in the full descriptive name of the fiduciary legally entitled to institute a proceeding on behalf of such person.

In the event of a variance between the name set forth in the notice of deficiency or liability and the correct name, a statement of the reasons for such variance shall be set forth in the petition. (See Rules 4, 7, and 23.)

The Commissioner shall be named as the respondent.

STATEMENT

The taxable years in question are 1942 to 1946, inclusive. For these years taxpayer filed separate individual tax returns with the Collector of Internal Revenue, Baltimore, Maryland. Taxpayer's wife filed no returns for this period. (Pet. 23.) The Commissioner determined deficiencies for the years involved, and sent a deficiency notice which was addressed to "Mr. Joseph N. Romm and Mrs. Helen K. Romm" at their correct address. (R. 5.)[3] The petition for review by the Tax Court, which contested the correctness of the Commissioner's determination in numerous respects, was brought in the names of taxpayer

[3] "R." references are to the appendix to taxpayer's brief in the Court of Appeals.

and his wife, but with taxpayer's wife appearing specially only because of the inclusion of her name in the notice of deficiency. (R. 1-5.) The Commissioner conceded, both in the Tax Court and in the Court of Appeals, that, inasmuch as taxpayer had filed separate individual returns for the period in question, only he was liable for the deficiency. (Pet. 12.) The Court of Appeals determined that, while the Tax Court had committed an inadvertent error in not limiting liability to the husband, the Tax Court had jurisdiction and that no reversible error had been committed. (Pet. 13.)

Although taxpayer has conceded the propriety of determining his income for the period involved by the net worth method (Supp. R. 33)[4] and the parties stipulated as to the correctness of the figures used in the net worth analysis (Supp. 34-41), taxpayer contends that the Tax Court and the court below erred in finding that increases in his wife's assets during the period involved were includible in the net worth analysis determining his income. (Pet. 4, 8.) The parties stipulated that as of December 31, 1941, taxpayer's wife had certain bonds and savings accounts in her own name totalling $2,258.95, and these assets increased until they totalled $9,066.94 as of December 31, 1946. (Supp. R. 34-36, Pet. 14-15, 26.) The Tax Court determined that the total of the assets in the wife's name as of December 31, 1941, adequately represented all her property as of that date,

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[4] "Supp. R." references are to the appendix to the Commissioner's brief in the Court of Appeals.

and that with two exceptions increases in the wife's assets during the taxable period were attributable to taxpayer's income. (Pet. 34-35.) The court below affirmed. (Pet. 14-16.)

The parties also stipulated that during the taxable years taxpayer had given his wife $100 per week, or $5,200 per year, for maintaining the household and defraying other personal expenses and that such sums were used for that purpose. (Supp. R. 41.) Taxpayer contends that the increases in his wife's assets during this period should not have been included in his net worth analysis because they were attributable to the $5,200 per year which he gave her and which had already been added to the increases in his own net worth in determining taxable income. (Pet. 4, 8.)

On August 11, 1954, or approximately two and one half months prior to the issuance of the deficiency notice, taxpayer made a payment toward satisfaction of the asserted deficiencies for 1946. (Pet. 30, Supp. R. 32.) Both the Tax Court and the court below held that the fraud penalty under Section 293(b) of the Internal Revenue Code of 1939 was properly computed on the basis of the deficiency on the original return, instead of on the basis of the tax remaining due after this payment was made. (Pet. 20-21, 35.)

The court below sustained the Tax Court's decision except in two minor respects.[5]

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[5] The first ordered the Tax Court to correct the inadvertent inclusion of the wife in its decision. The second allocated a $831.24 payment to principal of the deficiency, rather than to the fraud penalty, thus reducing interest. (Pet. 21-22.)

ARGUMENT

1. The court below was correct in holding that the Tax Court had jurisdiction to decide this case and that its failure to limit liability to taxpayer was not prejudicial to him. The deficiency notice was mailed to taxpayer and his wife, at their correct address. Although the deficiency notice erroneously stated that the returns filed were joint returns (R. 7-8) taxpayer was not misled thereby since a joint return imposes joint and several liability upon each spouse. Section 51(b) of the Internal Revenue Code of 1939, *supra*. Indeed, taxpayer contested the Commissioner's determination on the merits before the Tax Court, and raised this jurisdictional issue for the first time before the Court of Appeals. (Pet. 5.) Since the deficiency notice was mailed to taxpayer, received by him, and a petition was filed within ninety days, the Tax Court had jurisdiction to determine a deficiency against him. Section 272(a), Internal Revenue Code of 1939, *supra*.[6]

The decision below conflicts neither with the decision of this Court in the case of *Hulburd* v. *Commissioner*, 296 U.S. 300, nor with the Second Circuit's decision in *Bendheim* v. *Commissioner*, 214 F. 2d 26. In *Hulburd*, a deficiency was asserted against an executor who had been discharged, and under state law was no longer subject to assessment in his fidu-

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[6] There was full compliance with Tax Court Rule 6, *supra*, which is a procedural rule requiring a petition to be brought in the same names as those listed on the notice of deficiency.

ciary capacity; the executor petitioned to the Board of Tax Appeals on the ground that the assessment was invalid because the estate had been settled and the executors discharged. Here the proposed deficiency was asserted against the taxpayer, who contested the merits before the Tax Court. The *Bendheim* case held only that a deficiency notice is invalid where the entire proposed deficiency had previously been paid. Similarly, the Board of Tax Appeals and Tax Court decisions cited by taxpayer (Pet. 6-7) have no bearing on this point. And there are numerous decisions of the Courts of Appeals holding that formal defects in a deficiency notice are immaterial where not misleading, and that in any event such defects may be waived. *Commissioner* v. *Stewart*, 186 F. 2d 239 (C.A. 6th); *Olsen* v. *Helvering*, 88 F. 2d 650 (C.A. 2d); *McCarthy Co.* v. *Commissioner*, 80 F. 2d 618 (C.A. 9th), certiorari denied, 298 U.S. 655; *Buzard* v. *Helvering*, 77 F. 2d 391 (C.A. D.C.); *Commissioner* v. *Nichols & Cox Lumber Co.*, 65 F. 2d 1009 (C.A. 6th); *Haag* v. *Commissioner*, 59 F. 2d 516 (C.A. 7th); *Commissioner* v. *New York Trust Co.*, 54 F. 2d 463 (C.A. 2d), certiorari denied, 285 U.S. 556; *Burnet* v. *San Joaquin Fruit & Investment Co.*, 52 F. 2d 123 (C.A. 9th).

2. The question of whether the Commissioner properly included increases in the wife's assets during the taxable years in the computation of taxpayer's net worth is one of fact, and the court below correctly affirmed the Tax Court's determination.

The taxpayer apparently bases his contention be-

fore this Court [7] on the ground that the increases in his wife's assets during the taxable period stemmed from the $100 a week given her by her husband, and that these amounts had already been included in determining his taxable income (Pet. 4, 8); in other words, that the wife was able to save substantial amounts from her household allowance, and the increases in her assets during the taxable period represented these savings. This is primarily a question as to the credibility of the testimony presented, and was properly decided by the Tax Court. The court below found no error in this determination, and pointed out (Pet. 15) that the testimony of the wife "contained much inconsistency". Taxpayer seems incorrectly to contend (Pet. 8) that the Commissioner had the burden of showing that the wife had received funds from her husband in excess of the $5,200 a year. This Court has often recognized that the Commissioner's findings have a presumption of correctness, and the taxpayer has the burden of proving them wrong. See *Welch* v. *Helvering*, 290 U.S. 111, 115; *Old Mission Co.* v. *Helvering*, 293 U.S. 289, 294; *Helvering* v. *Taylor*, 293 U.S. 507, 515-516; *Commissioner* v. *Heininger*, 320 U.S. 467, 475. The Tax Court was clearly correct in holding that taxpayer did not sustain this burden, and the court below was correct in affirming its determination.

3. The court below did not err in holding that the

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[7] Before the Tax Court and the Court of Appeals, taxpayer also contended that these increases stemmed from savings of the wife in earlier years, but this contention has apparently been abandoned.

addition to tax for fraud imposed under Section 293 (b), Internal Revenue Code of 1939, *supra*, attaches to the entire amount by which the tax shown on the original return was understated, unreduced by a payment made shortly prior to the mailing of the deficiency notice.

Section 293(b) provides that in the case of fraud there shall be an addition to tax of "50 per centum of the total amount of the deficiency". Taxpayer contends (Pet. 9-10) that inasmuch as Section 271(a), Internal Revenue Code of 1939, *supra*, defines "deficiency" as excess of the tax legally due over the total of the tax shown on the return and amounts previously collected, then the 50 per cent addition should be computed only with reference to the tax remaining unpaid as of the time of the proposed assessment. This contention is without merit, and has been repeatedly rejected. *Middleton* v. *Commissioner*, 200 F. 2d 94 (C.A. 5th); *Still, Inc.* v. *Commissioner*, 19 T.C. 1072, affirmed *per curiam*, 218 F. 2d 639 (C.A. 2d); *Eck* v. *Commissioner*, 16 T.C. 511, affirmed *per curiam*, 202 F. 2d 750 (C.A. 2d), certiorari denied, 346 U.S. 822; *Sherin* v. *Commissioner*, 13 T.C. 221, *Hirschman* v. *Commissioner*, 12 T.C. 1223, appeal dismissed, January 10, 1950 (C.A. 2d); *Wilson* v. *Commissioner*, 7 T.C. 395.[8] As the court

[8] *Schwarzkopf* v. *Commissioner*, decided July 10, 1957 (C.A. 3d) (57-2 U.S.T.C., par. 9816), cited by taxpayer (Pet. 10), involved the applicability (not the computation) of the addition to tax for substantial underestimation of estimated tax under Section 294(d)(2) of the Internal Revenue Code of 1939 and possesses no present relevancy.

below pointed out (Pet. 21) the result of such an interpretation would be that a fraudulent taxpayer could easily avoid the imposition of the 50 per cent addition to tax by paying the tax due as soon as an investigation should be commenced, and thereby "make sport of the so-called fraud penalty".

CONCLUSION

The decision of the court below is correct, there are no conflicting decisions, and further review is not warranted. The petition for a writ of certiorari should be denied.

Respectfully submitted,

J. LEE RANKIN,
Solicitor General.

CHARLES K. RICE,
Assistant Attorney General.

I. HENRY KUTZ,
MILDRED L. SEIDMAN,
Attorneys.

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